AMERICAN COUNCIL OF LIFE INSURERS
FINANCIAL SECURITY FOR LIFE

Statement of American Council of Life Insurers

on

"Planning for Long-Term Care"

before the

Health Subcommittee of the House Energy and Commerce Committee of the United States Congress

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My name is Gregory F. Jenner, and I am Executive Vice President, Taxes and Retirement Security, for the American Council of Life Insurers (ACLI). The ACLI is a Washington D.C.-based national trade association representing more than 350 member companies that offer life insurance, annuities, pensions, long-term care insurance, disability income insurance and other retirement and financial protection products. I am responsible for policy development, formulation and implementation with respect to all tax, pension and retirement security issues, and serve as the senior tax expert for and principal liaison on those issues between member companies and Congress, the IRS, and the Treasury Department. Prior to joining ACLI, I served as Acting Assistant Secretary of the Treasury for Tax Policy.

We are delighted that this Subcommittee is addressing an important issue facing this nation – long-term care. We applaud Chairman Nathan Deal (R-Georgia) and Ranking Member Sherrod Brown (D-Ohio) for drawing attention to this matter, and we are pleased to discuss with the Subcommittee the important role that private long-term care insurance plays in helping to provide the retirement security of millions of middle-income families, and what Congress can do to help those families prepare for their retirement.

The Need for Long-Term Care and the Role of Long-Term Care Insurance

ACLI's recently-updated study on long-term care in the "Baby Boom" generation notes that about 55 percent of those 85 and older require some form of long-term care, and about 19 percent of all seniors suffer from some degree of chronic impairment. By 2050, it is estimated that up to 5.4 million seniors will need the services of a nursing home – the most costly form of long-term care – and another 2.4 million will require home health care[1].

[1] ACLI 2005 Study: "Long-Term Care Insurance or Medicaid: Who Will Pay for Baby Boomers' Long-Term Care?"

The cost of long-term care is high and increasing, averaging $70,912 annually for a private room or $62,532 annually for a semi-private room in a nursing home; $25.32 per hour for a visit by a home health aide; and an average annual *base* rate of $32,294 for the services of an assisted living facility.[2] Since 1990, the price of nursing home care has increased at an average annual rate of 5.8 percent – almost double the overall inflation rate.

Total annual expenditure on long-term care for the elderly is estimated to be $135 billion, which accounts for over 9.7 percent of total spending on health care for persons of *all* ages. This is roughly 1.2 percent of the U.S. GDP. Of greater significance is that the elderly account for a disproportionately large percentage of total health care expenditures -- 36.3 percent of expenditures -- while accounting for only 12.4 percent of the population.[3] Because baby boomers are aging and the cost of care is increasing, total spending on nursing home care is expected to more than triple over the next 25 years and to increase more than five-fold in the next 45 years. These increases will place a crushing burden on Medicaid and ultimately on taxpayers, most of whom are working-age adults. Currently, there are about five working-age adults per senior, but by 2030, there will only be 2.9 – a 40 percent decline. This decline will occur while both the need for and cost of long-term care increase.

At the same time, life expectancy has increased dramatically. Unfortunately, increased longevity comes at a price: the likelihood that more seniors will require long-term care. Given this increasing possibility that the typical senior will require long-term care, and given the escalating costs of that care, whether elderly boomers enjoy a comfortable retirement or suffer economic hardship may depend largely on their ability to afford such long-term care. Most boomers have not planned for this reality and face the prospect of paying large sums out-of-pocket or relying on Medicaid. A February 2006 survey conducted

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[2] Genworth Financial 2006 Cost of Care Study
[3] U.S. Department of Health and Human Services; U.S. Census Bureau.

by Public Opinion Strategies found that 65% of Americans have made no plans for their own or for family members' long-term care needs.[4] Moreover, Medicaid currently only covers the cost of long-term care after a senior has spent down virtually all assets and retirement income. Neither option is very appealing and may leave seniors and their spouses impoverished, with few long-term care choices.

Private insurance currently pays for 8 percent of total nursing home expenditures but 36 percent of overall health expenditures. There is clearly a large gap in the financing of long-term care services that private insurance can fill. Our goal, as well as the goal of Congress, should be to find ways for the average consumer to plan for the ever-increasing need for long-term care through the private sector instead of through government programs.

If three-quarters of individuals between the ages of 40 and 65 who can afford long-term care insurance were to purchase and maintain a policy throughout their senior years, then by 2030, annual savings in Medicaid nursing home expenses would total $19 billion, and annual savings in out-of-pocket expenses would total $41 billion. Given this, it is clear more needs to be done to convince the Baby Boom generation of the need for this type of investment NOW.

The Evolving Long-Term Care Insurance Market

Both the individual and group (employer-sponsored) segments of the long-term care insurance market are evolving and growing. The American Council of Life Insurers, with the assistance of America's Health Insurance Plans, recently surveyed long-term care insurance providers and found that:

[4] Public Opinion Strategies 2006 Survey

- The market has grown to nearly $7 billion in premiums, and now covers over 5 million people.

- Between 2003 and 2004, the individual long-term care insurance market grew 7.5 percent and the group market grew 25 percent.

- The amount paid out in claims has also increased, with carriers paying $2.1 billion in benefits in 2004, about 20 percent more than in the previous year.[5]

Because private long-term care insurance is priced on the assumption that an individual will hold the same policy and pay the same premium until he or she needs long-term care, premium rates vary depending on the age of the policyholder at policy issue and the specific benefits and coverage chosen. Additionally, younger candidates for policies are much more likely to pass underwriting screens than are older candidates. For these reasons, consumers are encouraged to purchase insurance while they are in their 40s and 50s, when premiums are lower and more affordable. The typical buyer of long-term care insurance is aged 55-60 (although the average age of those who enroll in group plans is in the forties), married, college educated, with an annual income in excess of $50,000. Women are more likely to buy coverage than men.

Although the market for long-term care insurance is growing, most Americans have not yet purchased this insurance protection. Impediments to even greater market growth include competing demands for discretionary income, limited incentives to purchase long-term care insurance, impediments to streamlined products that will lower costs to consumers, and the lack of awareness of the need to plan for potential long-term care expenses.

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[5] ACLI (2005)

Long-term care insurance products continue to evolve to give policyholders more choices and flexibility at the time they need care. When long-term care insurance was first offered, over 30 years ago, most plans only covered stays in skilled nursing facilities. Since the mid 1990s, more flexible care options and consumer protections have become available. Today, most policies provide coverage for care received at home, in an adult day care facility, in an assisted living facility, or in a nursing home. Additionally, plans are now guaranteed to be renewable, have a 30- day "free look" period, offer inflation protection, cover Alzheimer's disease, have a waiver of premium provision, and offer unlimited benefit periods. Benefits are paid when a person needs help with two or more activities of daily living (such as eating, dressing, or bathing) or is cognitively impaired.

Some of the innovative benefits and financing arrangements that companies now provide include:

- Caregiver training benefits that cover the cost of training a person (friend or family member) who will then care for the insured in the insured's home on an unpaid basis. The benefit is usually equivalent to five times the daily benefit and not subject to an elimination period.

- "Per diem" or cash benefits that pay without regard to cost of services or pay benefits in cash. These benefits make it easier to understand and file claims and allow the claimant greater flexibility to utilize informal caregivers.

- Shared lifetime maximum benefit pools that allow a policyholder who uses up all of his or her benefits to tap into a spouse's lifetime maximum, or to leave any unutilized benefits at death to a surviving spouse.

- Independence support benefits that pay for home modifications and personal emergency alert systems that would enable a policyholder to remain in the home for a longer period of time.

- Death benefits that will return all or a portion of past premium payments in the event the policyholder dies before utilizing long-term care insurance benefits.

- International benefits that pay for services received in a foreign country.

Congressional Involvement in Long-Term Care Insurance Product Innovation

The United States Congress will continue to play an important role encouraging the evolution of the long-term care insurance marketplace. Significant changes were enacted earlier this year and others are pending as we speak. We look forward to continuing our excellent relationship with the House Energy and Commerce Committee and other committees of the House to encourage greater flexibility and innovation in the long-term care marketplace.

- **Long-Term Care Partnerships**

Earlier this year, Congress passed and the President signed into law the Deficit Reduction Act of 2006. That bill expanded the ability of the states to enter into the Long-Term Care Partnership program, which will ultimately ease the burden on state Medicaid budgets and on individual consumers. We thank and congratulate the members of this Committee for their help and support.

These public-private Partnerships, currently operational in four states, allow consumers to purchase long-term care policies whose benefits must be fully utilized prior to qualifying for Medicaid. Many states are now looking to utilize this new public policy opportunity by seeking approval from the Department of Health and Human Services for an amendment to their State Medicaid plan in order to implement a Partnership program. Insurers anticipate that Partnership programs will provide a greater incentive to purchase long-term care insurance in those states that choose to participate.

ACLI is currently working to implement these partnerships in all 50 states and the District of Columbia. This is an excellent example of an innovative program that offers a "win-win" opportunity for the states and consumers.

- **Flexible Retirement Security Proposal**

I have been asked to focus primarily on innovations in long-term care insurance products. It is my pleasure to call to the Committee's attention a proposal pending before the Congress that we believe would have significant beneficial effects on the marketplace. That provision is contained in the House version of the pension bill now in conference.

It comes as a surprise to no one that the tax code has considerable effect on the pricing of insurance products and the ability of companies to create innovative solutions that address the needs of consumers. Provisions of the tax code prevent companies from offering policies that combined the features of an annuity with the benefits of long-term care insurance.

Removing this impediment would likely result in increased utilization of long-term care insurance. The reason had to do with consumer attitudes toward insurance. Most Americans recognize the need to insure against risk, whether it is the risk of an early demise, a traffic accident, or the risk that a person will need long-term care. But most people have only limited resources, and many are unwilling to purchase insurance where the policy offers no accumulation feature; i.e., where the premiums paid are lost to the policyholder if the insurance is not used. Without some sort of "savings" feature, consumers with limited resources often were not willing to purchase insurance, including long-term care insurance, even though they recognize its importance.

So why did the tax law prohibit long-term care insurance from offering an accumulation feature, such as an annuity? Quite frankly, there was no good reason. Therefore, we worked with members and staff of the Committee on Ways and Means to develop a provision that would permit the combination of an annuity and long-term care insurance in one policy (and clarify that life insurance and long-term care could also be combined). That provision is in the House version of the pension bill now pending in conference. We would like to thank Chairman Thomas for including it in the bill, and also thank Mrs. Johnson of Connecticut, Mr. English of Pennsylvania, and Mrs. Tubbs Jones of Ohio for their hard work and support. We would also encourage the members of this Committee to actively support inclusion of this provision in the final pension conference report.

This proposal would create more flexibility and choice for American consumers. During working years, individuals could accumulate assets in an annuity; at retirement, depending on the needs of the individual, that annuity could be used to provide lifetime income. A long-term care insurance benefit within the annuity would pay for long-term care services. For the long-term care/life insurance combination, the life insurance would serve its critical function of death protection, while also being available to provide funds for payment of long-term care costs.

Although life insurance, endowment and annuity contracts can be exchanged without tax if certain conditions are met, currently, long-term care contracts and riders are not included in the tax-deferred exchange provisions. The law should be updated to include long-term care contracts and riders among the permitted tax-deferred exchangeable insurance products.

This is an excellent example of the law unintentionally standing in the way of innovation in the marketplace. We will continue to work with you in the Congress to remove such unnecessary barriers to innovation. We believe that, with your help, our industry can adapt and accommodate the changing needs of the American consumer.

- **Tax Incentives**

Cost is a major reason why more Americans have not yet purchased long-term care insurance. Although product combinations may prove to be an attractive alternative to stand alone long-term care insurance for some individuals, an even more broadly appealing and effective solution to the financing of long-term care would be the passage of measures that reduce the cost of long-term care insurance, particularly for moderate-income individuals, the persons who need the protection of long-term care insurance the most. Partnerships and combination products can only go so far to accomplish this. If Congress determines it is important that individuals of moderate means are protected in this fashion, there are steps that can be taken.

Although not strictly a product innovation, we would encourage Congress to provide individuals with a phased-in above-the-line federal income tax deduction for the eligible portion of the premiums they pay to purchase long-term care insurance. This would create a more even playing field between long-term care insurance and health insurance (which we all agree is crucial). In addition, Congress should permit long-term care insurance policies to be offered under employer-sponsored cafeteria plans and flexible spending accounts. This benefit is allowable for similar accident and health coverage and there is no strong policy consideration to justify the exclusion of long-term care insurance. Finally, we would urge that individuals be permitted to exchange tax free one qualified long-term care policy for another long-term care policy better suited to the insured's needs.

Allowing individuals to pay for their long-term care insurance premiums through cafeteria plans and flexible spending accounts, as well as through flexible retirement security combination products, will provide a range of options both inside and outside the employment context. Such measures could go far to help control rising long-term care costs, rising long-term care needs, and rising strains on the Medicaid budget. Individuals will have the ability to pay privately and have the ability to choose a variety of services and care settings best suited to their needs.

- **Other Related Legislation**

In this spirit, other members of Congress have been likewise engaged in the discussion of how to encourage individuals to plan for their long-term care costs. For example, Rep. Terry (R-NE), who serves on this Committee, has introduced a bill that would allow individuals to exclude from gross income distributions made from their individual retirement accounts, 401(k), or 403(b) plans that are used to pay for long-term care insurance premiums for themselves or their spouses.

An optional federal charter for life insurers, including long-term care insurers, would also help long-term care insurance innovations reach consumers in a more timely and cost-effective manner. Senators Sununu and Johnson recently introduced S. 2509, which would create an optional federal charter. Today, it can take up to two years for an innovative long-term care insurance product to be approved in all 50 states and the District of Columbia and be sold nationally. Consumers should have the benefit of a timely array of long-term care product choices that best meet their needs.

- **Federal Government Long-Term Care Insurance Program**

The federal government and the states have also recognized the need to educate individuals in the workplace about planning for their future long-term care needs. The federal government, by Act of Congress, has taken the lead and set the example for other employers by offering federal employees and their families the protection of long-term care insurance. Through this program, federal employees are able to help protect their retirement savings from a long-term care event and will have the choice of providing care for themselves or a family member in the home, through assisted living or in a nursing home.

- **Other Innovative Solutions**

Although we are focused today on innovations in long-term care insurance, the nature of governance is that you (and we) will likely be focused elsewhere tomorrow. But solutions to the pressing problems of financing retirement and longevity should not be viewed as a snapshot. Our industry is committed to examining these issues on an ongoing basis. As important, we need to know that, if we develop an innovative idea, we can come back to this Committee and win your support. We, as an industry, look forward to a constructive partnership with the Congress in developing and implementing creative solutions to this country's retirement needs.

Private Long-Term Care Insurance: An Important Part of the Answer

In conclusion, we believe that protection and coverage for long-term care is critical to the economic security and peace of mind of all American families. Private long-term care insurance is an important part of the solution for tomorrow's uncertain future. As Americans enter the 21st century, living longer than ever before, their lives can be made more secure knowing that long-term care insurance can provide choices, help assure quality care, and protect their hard-earned savings when they need assistance in the future. We also believe that the costs to Medicaid – and therefore to tomorrow's taxpayers – will be extraordinary as the baby boom generation moves into retirement, unless middle-income workers are encouraged to purchase private insurance now to provide for their own eventual long-term care needs.

Congress has encouraged the American public to insure themselves against the need to pay for long-term care by adopting the Deficit Reduction Act of 2006 and allowing for the expansion of LTC Partnerships. Congress should build on that momentum by encouraging the development of innovative products such as combination annuity/long-term care insurance products and life/long-term care insurance products. Further, Congress should include long-term care insurance products in cafeteria plans and flexible spending accounts, and consider other tax incentives to encourage the sale of these products.

Again, ACLI looks forward to working with this Subcommittee to help Americans protect themselves against the risk and high cost of long-term care.